

Proposed Regulation 1603, *Taxable Sales Of Food Products*

Initial Statement of Reasons Overview/non-Controlling Summary

Proposed Regulation 1603 is proposed to be promulgated to interpret, implement and make specific Revenue and Taxation Code sections 6011 and 6012. The regulation proposed by Staff recommends that subdivision (g) of Regulation 1603 be expanded to clarify the current application of tax, as follows:

- An amount, whether designated as a tip, gratuity, or service charge, is optional and not subject to tax when it is added to the bill by the customer or otherwise left by the customer in payment over and above the actual amount due the retailer.
- An amount, whether designated as a tip, gratuity, or service charge, is presumed to be mandatory and subject to tax when added to the bill by the retailer. Amounts negotiated between the retailer and the customer in advance of a meal or events are mandatory. A statement printed on a menu, advertisement or a brochure advising the customer that a tip, gratuity, or service charge will or may be added to the bill when a group of people exceeds a specified number is evidence that the charge is mandatory and part of the gross receipts from the sale of the meal, food, or drinks. As such, it is subject to tax.

Subdivision (g) would also incorporate and replace the provisions of current subdivision (h)(3)(E) to further clarify that the above provisions apply to retailers selling food and beverages, including restaurants, hotels, caterers, boarding houses, soda fountains, drive-ins, and similar establishments. Staff's proposed language is attached as Exhibit 2.

Specific Purpose

The purpose of the proposed regulation is to interpret, implement, and make specific Revenue and Taxation Code sections 6011 and 6012. This regulation is necessary to provide guidance to taxpayers affected by this statute.

Factual Basis

Proposed Regulation 1603 discusses the application of tax to tips and gratuities and distinguishes between tips and gratuities that are at the customers discretion and tips and gratuities that are added to the bill by the retailer.

Pursuant to Government Code section 11346.5(a)(8), the Board of Equalization finds that the adoption of the proposed regulation will not have a significant adverse economic impact on private businesses or persons. The regulation is proposed to interpret, implement, and make specific the authorizing statutes. These changes will clarify the interpretation or administration of the sales and use tax laws. Therefore, the Board has determined that these changes will not have a significant adverse economic impact on private businesses or persons.